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IN THE

**SUPREME COURT OF THE
UNITED STATES**

OCTOBER TERM, 1944

No. 177

**J. M. LEDBETTER, JR., ADMINISTRATOR C. T. A. OF
THE ESTATE OF ROBERT L. STEELE, III, AND THE
STATE OF NORTH CAROLINA AND THE CLERK OF
THE SUPERIOR COURT OF BLADEN COUNTY, as
rel., AND FOR THE USE AND BENEFIT OF J. M.
LEDBETTER, JR., ADMINISTRATOR C. T. A. OF THE
ESTATE OF ROBERT L. STEELE, III, Petitioners,**

vs.

**FARMERS BANK & TRUST COMPANY, A CORPORA-
TION, AND FEDERAL RESERVE BANK OF RICH-
MOND, A CORPORATION.**

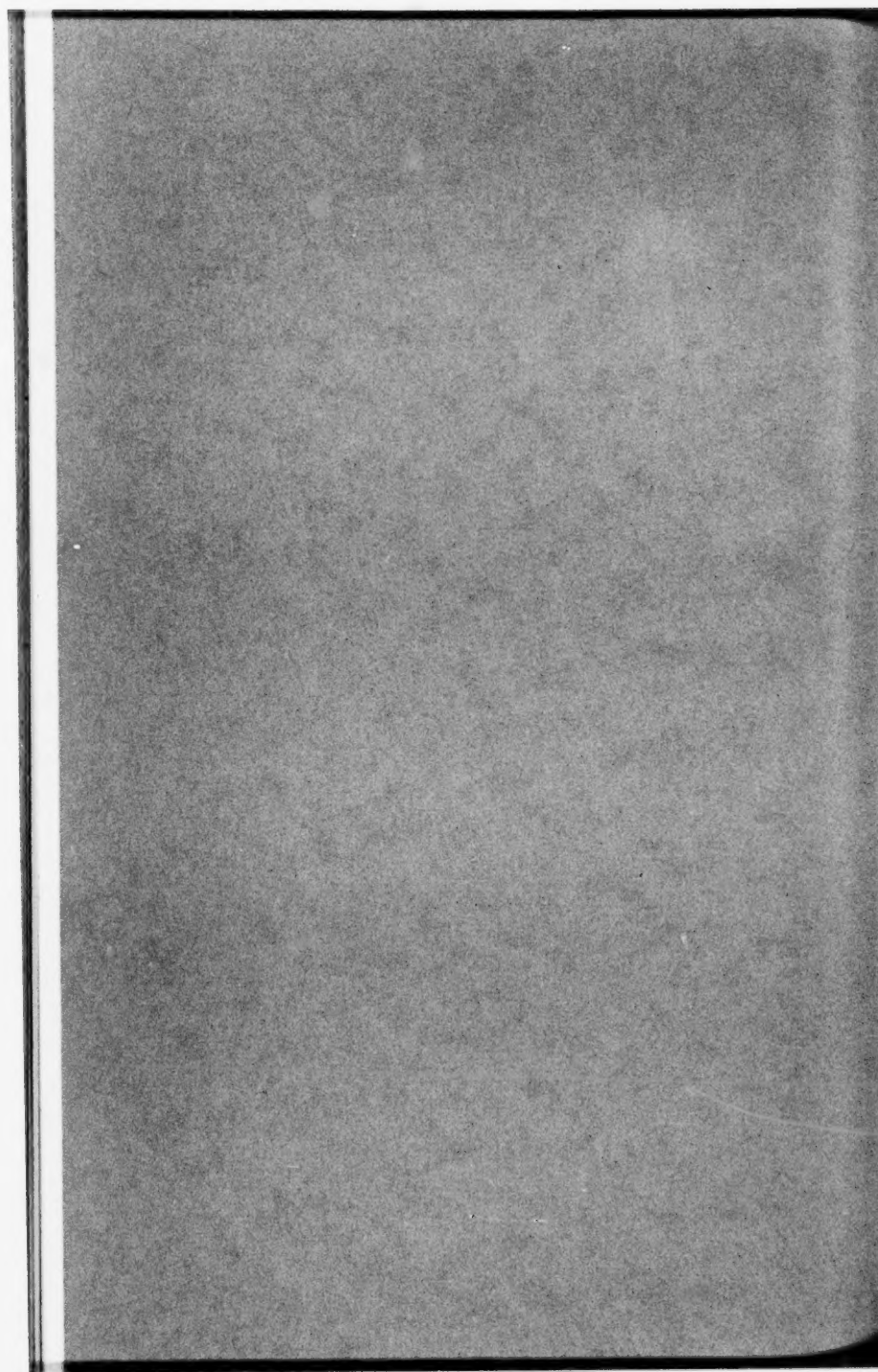
**Brief of Petitioners In Reply to Brief of Respondents
Opposing Petition For Writ of Certiorari.**

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I

RESPONDENTS' STATEMENT OF FACTS

On page two of their brief, respondents say that we apparently rely upon the thesis that a receiver appointed in a foreclosure proceeding is the alter ego of the party upon whose motion he is appointed. We are afraid that respondents have misapprehended our position in this matter, for (though we do not desire to waive the right to urge this Court to hold that the mortgagee should be liable for loss of property in the hands of the receiver because the receivership is for his benefit) we do not claim that the

receiver in most mortgage foreclosure actions is the alter ego of the mortgagee, but we have alleged in this case that the receiver acted according to the desires and directions of the mortgagees and not "with an impartial and independent discretion." The allegations that the receiver was acting according to the desires and the directions of the mortgagees distinguishes this case from the general case in which the receiver is an independent person between the parties. It is the direction and control of the receiver by the mortgagees which makes him in this case the alter ego of the mortgagees.

On page three of their brief, respondents object to the allegations that the receiver did not act with an "impartial and independent discretion" on the ground that these "are mere words of characteristization and color." While, perhaps, if these words stood alone, they would be objectionable, still, since they immediately follow the allegation that the receiver was acting in conformity "the desires and directions" of the mortgagees, these words serve to illustrate and illuminate the allegations as to control. Quite naturally we would not allege "any act done by the receiver which showed partiality" (respondents' brief, page 3), for an allegation of such an act would be an allegation of an evidentiary fact, while we must allege the ultimate facts to be proved. *McAllister v. Kuhn*, 96 U. S. 87, 24 L. ed. 615; *Indianapolis & St. L. R. Co. v. Horst*, 93 U. S. 91, 23 L. ed. 898; *Fleishman Const. Co. v. U. S. use of Forshberg*, 270 U. S. 349, 70 L. ed. 624, 46 S. Ct. 284; *Lucas v. Federal Reserve Bank of Richmond*, 59 F. 2d 617; *Knight v. Little*, 217 N. C. 681, 9 S. E. 2d 377; *Hawkins v. Moss*, 222 N. C. 95, 21 S. E. 2d 873; *Lefkoff v. Sicro*, 189 Ga. 554, 6 S. E. 2d 687, 133 A. L. R. 738; *Mitchell v. Frederick*, 166 Md. 43, 170 A. 733, 92 A. L. R. 1412; *Zuniga v. Evans*, 87 Utah 198, 48 P. 2d 513, 101 A. L. R. 532; *McIntosh*, *North Carolina Practice and Procedure*, page 349; 41 *Am. Jur.* 292-293, Pleading, Secs.

7 and 8; 49 C. J. 40, Pleading, Sec. 16; *Id.*, 88, Pleading, Sec. 85. The ultimate fact to be proved is the control of the receiver by the mortgagee. *Dillon v. Winston-Salem*, 221 N. C. 512, 20 S. E. 2d 845.

II

THE APPLICATION OF THE RULES OF CIVIL PROCEDURE

We have never conceded that the motion for leave to amend was not a motion under Rule 15 as respondents indicate on page 5 of their brief. In fact, question two of the questions presented (Petition, page 5) indicates that one of the questions which we would ask this Court to decide if it granted the petition for certiorari would be whether this motion was a motion under Rule 15, Rule 59 or Rule 60. Furthermore, the Circuit Court of Appeals (R. 19) gave that as an alternative ground for its decision, if the motion is not one controlled by Rule 59. We did not go into this question more thoroughly because we did not think it proper in a petition and the brief thereon, however material it might be in a brief on the merits. In this connection, we think it worthy of remark that Rule 59 only applies to motions for a new trial, and, as was pointed out in the dissenting opinion in *Safeway Stores v. Coe*, 78 U. S. App. D. C., 136 F. 2d 771, 57 U. S. P. Q. 516, a new trial has been universally held to be a re-examination of an issue of fact. See 39 *Am. Jur.* 33, New Trial, Sec. 2; *Wheeling & Lake Erie Ry. Co. v. Ritcher*, 131 Ohio St. 433, 3 N. E. 2d 408, 410; *Garden City Feeder Co. v. Commissioner of Internal Revenue* (C. C. A. 8th), 75 F. 2d 804. Hence it would seem that Rule 59 could not apply to a motion to amend or vacate a judgment where there had been no trial of an issue of fact. The mere fact that the motion, if allowed, would have resulted in the vacation of the judgment does not make it a motion for a new trial under Rule 59. *Leishman v. Associated Electric Company*, 318 U. S. 203, 87 L. ed. 714, 63 S. Ct. 543.

III

**THE FAILURE OF THE CIRCUIT COURT OF APPEALS
TO FOLLOW LOCAL DECISIONS**

Respondents argue that as a matter of law the mortgagees had no right to control the receiver. From that they draw the conclusion that he could not be controlled by the mortgagees. Their argument is similar to one that might be advanced that there had in fact been no murder because the defendant had no right to murder the deceased. We alleged the fact that the receiver was controlled by the mortgagees, and they countered with the proposition that the mortgagees had no right to control. We alleged facts which we think we should have been allowed to prove in order to show the reality of the situation under the doctrine of the following cases:

Unemployment Compensation Commission v. Coal Co. (1939) 216 N. C. 6, 3 S. E. 2d 290; *Mills v. Mutual Building & Loan Association* (1940), 216 N. C., 664, 6 S. E. 2d 549; *Smith v. Greensboro Joint Stock Land Bank* (1938), 213 N. C. 343, 196 S. E. 481; *Peedin v. Oliver* (1943), 222 N. C. 665, 24 S. E. 2d 519.

Furthermore, when we alleged that the receiver acted in accordance with the desires and directions of the mortgagees, we alleged no less than was proved in *Dillon v. Winston-Salem*, 221 N. C. 512, 20 S. E. 2d 845. In that case there was no evidence of any legal right on the part of the passenger to control the driver, but, nevertheless, the passenger was held liable for the negligence of the driver on proof that the driver was driving the automobile to the place to which he was directed by the passenger. We submit that when the Circuit Court of Appeals failed to reverse the district court, it likewise failed to follow the decision of the Supreme Court of North Carolina in *Dillon v. Winston-Salem*, *supra*.

Respondents also contend that, if there be any distinction in other jurisdictions between a receiver appointed in a mortgage foreclosure action and any other action, the distinction does not exist in North Carolina because in North Carolina the same statutes govern the appointment of mortgage receivers and other receivers. It is true that the same statutes do govern the appointment of both, but that is a matter of *procedure* and not of *substance*. And the distinction made between the two kinds of receivers is that one is acting for the benefit of the mortgagee, and the other is holding the property for the general creditors. 2 Glenn, *Mortgages*, Secs. 172.1 & 187; 2 Clark, *Receivers*, Sec. 963(a); *Sorchan v. Mayo*, 50 N. J. Eq. 288, 23 Atl. 479. Furthermore, even the North Carolina statutes recognize that a receivership is for the benefit of the mortgagee and is against the mortgagor, for G. S., Sec. 1-504 (Michie's Code, Sec. 862, pp. 8 and 9, of Respondents' brief) provides for a bond "*payable to the adverse party.*" (Italics added.)

In this connection, *Kane v. Roxy Theatres* (1933), 63 F. 2d 754; *DuParquet, etc., Co. v. Evans* (1936), 297 U. S. 216, 56 S. Ct. 412, 89 L. ed. 591; and *N. Y. Life Insurance Co. v. Fulton Development Co.* (1934), 265 N. Y. 348, 193 N. E. 169 (relied upon by Mr. Glenn as supporting the proposition that the receiver represents the mortgagee alone), show that the reality of the situation is that the possession of the mortgage receiver is the possession of the mortgagee.

IV

RESPONDENTS' AUTHORITIES EXAMINED

As we pointed out in the petition and brief in support of it, pages 8 and 17-19, there are only 6 cases outside of North Carolina with holdings on the liability of a mortgagee for the loss of property in the hands of a receiver. The cases relied upon by respondents, with the exception of the two mentioned in the petition, contained nothing more

than dicta to that effect. As a matter of fact, the case of *Fountain v. Stickney*, 145 Iowa 167, 123 N. W. 947, 139 A. S. R., 41, had nothing to do with the matter for which it was cited. That case involved a demurrer by a receiver in a damage suit brought against the receiver by a person injured by the corporation before the receivership. The court upheld the demurrer without considering whether or not it would have done so had the plaintiff alleged leave of court to sue.

The Tennessee statute, Williams Code of 1934, Secs. 10-559, does not, as contended by respondents, furnish the basis for the decisions in the Tennessee Cases. The statute provides that the "*receiver or the complainants*" shall give bond. Obviously, if the complainant did not give bond under this statute and the receiver did, the complainant would not, merely by virtue of the statute, be liable for the failure of the receiver faithfully to discharge his duties. And the cases of *Terrell v. Ingersoll*, 78 Tenn. 652, and *Downs v. Allen*, 78 Tenn. 77, make no mention of any bond whatever. But even if the complainants had given bond under the statute, they would be liable by virtue of the statute, only to the extent of the bond. Hence, the court in stating the rule in those cases must have been stating the common law rule rather than a statutory rule, for the court stated generally that "the complainant is liable for all losses occasioned by the neglect of the receiver to do his duty."

In *Atlantic Trust Co. v. Chapman*, 208 U. S. 360, 28 S. Ct. 406, 52 L. ed. 528, 13 Ann. Cas. 1155, which was a contest between the receiver and the mortgagee's trustee as to which should pay the receivership expenses, the Court seems to have been enforcing the rule that it is wrongful for the receiver to continue to operate at a loss, for it calls attention to the fact that the receiver was the only one who knew that there was likely to be a deficit. 208 U. S. at 373, 13 Ann. Cas. at 1159. See 2 Glenn, *Mortgages*, 982-983, Sec. 190.

In *Robinson v. Arkansas Loan & Trust Co.*, 74 Ark. 292, 85 S. W. 413, it did not appear either that the receiver was insolvent or that the bond was inadequate; and it would appear, too, that, without such a showing, the holding of the court is correct. But in any case, the authority of that case is weakened because the court failed to cite any cases upholding the other rule¹ though at that time *Sochran v. Mayo*, *supra*, *Downs v. Allen*, *supra*, and *Terrell v. Ingersoll*, *supra*, had all been decided, and they all contained holdings contrary to that adopted in the *Robinson Case*. (This might be an indication that the bond was sufficient, for otherwise, it would seem, the court would have cited the New Jersey and Tennessee cases.) On the other hand, only one case in the United States at that time, *Kaisar v. Kellar*, 21 Iowa 95, had held that the mortgagee is not liable, and the holding in that case is, as we pointed out in the petition (p. 9) and brief in suport (p. 18), distinguishable from that in this case.

Mitchell Machine and Electric Co. v. Sabin, 218 Ky. 289, 291 S. W. 381, relied upon by respondents, was decided on a question of jurisdiction. (Contra on that point: *Re Penny*, D. C., M. D. N. C., 10 F. Supp. 638); and in *City Savings Bank v. Carlon*, 91 Neb. 790, 127 N. W. 161, relied upon by respondents, the receiver was receiver of a corporation in liquidation, and plaintiff, a stranger to the receivership action, was injured by the tort of the receiver. In that case, there was neither an action on the bond, an allegation of the insolvency of the receiver nor an allegation that the receiver acted under control of the defendant.

The dictum in *O'Connell v. St. Louis Joint Stock Land Bank*, 170 Ark. 778, 281 S. W. 385, is explained by the doctrine of stare decisis since it relied upon the *Robinson Case*, *supra*.

¹ *Carr v. Eel River & Eureka R. Co.*, 93 Cal. 366, 33P. 213, 21 L. R. A. 354, 365.

State v. Whitehurst, 212 N. C. 300, 193 S. E. 657, 113 A. L. R. 740, is relied upon by respondents for the proposition that the receiver is a hand or arm of the court (a proposition that we do not deny). The language of the court is interesting (212 N. C. at 303):

"Thus it will be seen that, by repeated amendments, the scope of the statute has been gradually enlarged and its base progressively broadened. But at no time has it been made applicable, *ipsissimis verbis*, to receivers of insolvent corporations. Nor does it appear, under the rule of strict construction (25 R. C. L., 1076) that the statute is susceptible of the interpretation inclusive of such receivers.

"By the rule of strict construction, however, is not meant that the statute shall be stintingly or even narrowly construed (*S. v. Earnhardt*, 170 N. C., 725, 86 S. E., 960), but it means that everything shall be excluded from its operation which does not clearly come within the scope of the language used. *U. S. v. Wiltberger*, 5 Wheat., 76. *Criminal statutes are not to be extended by implication or equitable construction to include those not within their terms*, for the very obvious reason that the power of punishment is vested in the legislative and not the judicial department: It is the General Assembly which is to define and ordain their punishment. *Jennings v. Commonwealth*, 109 Va., 821, 63 S. E., 1080, 132 A. S. R., 946, 17 Ann. Cas. 64, 21 L. R. A. (N. S.), 265. Compare *S. v. Humphries*, 210 N. C., 406, 186 S. E. 473, and *S. v. Bell*, 184 N. C., 701, 115 S. E. 190." (Emphasis supplied.)

And later, p. 303: ". . . He is not an agent within the meaning of the embezzlement statute. *S. v. Hubbard*, 58 Kan., 797, 51 Pac., 290, 39 L. R. A., 860. . . ."

Respondents seek to minimize the authority of *Sorchan v. Mayo*, 50 N. J. Eq. 288, 23 Atl. 479, on the grounds that it was rendered by a one-man court, it has never been cited

but once,² it is cited by the text-writers as a minority holding, and the opinion itself acknowledges that it is at variance "with all the then extant American authority." (Respondents' brief, pp. 17-19.) Though *Vice Chancellor Pitney* may have been sitting by himself when he delivered that opinion and though it has never been cited but once, the opinion does not acknowledge that it is at variance "with all the then extant American authority." Nor is it, when it is referred to in textbooks, always mentioned in footnotes as "an exceptional case." (Respondents' brief, p. 18.) In 3 Jones, *Mortgages* (7th ed.), Sec. 1537a (3 Jones, *Mortgages*—8th ed.—Sec. 1954), it is said:

"Whether a mortgagee who nominates and secures the appointment of a receiver is responsible for his default is a question upon which there is a *conflict of authority*. On the ground that the receiver is appointed for and on behalf of all persons interested, it is contended that any loss arising from the default of the receiver must be borne, as between the parties, by the estate in his hands.³ (2 Daniell, Ch. Pr., pp. 740; 2 Maddock, Ch. Pr., p. 255; Kerr, Receivers, p. 64. These authorities all rely upon the single case of *Hutchinson*

² The fact that a case has never been cited does not detract from its effect as authority. *Ray v. Denver*, 109, Colo. 74, 121 P. 2d 886, 138 A. L. R. 1485.

³ It would seem that, as a matter of logic, if the receiver is appointed for the benefit of all parties, then the loss should be suffered by all and not merely by the mortgagor, which is the result if the loss fall on the estate, for the debt is still subsisting. Furthermore, in a mortgage receivership, the receiver is appointed for the benefit of the mortgagee. (*Sorchan v. Mayo*, *supra*; *Kane v. Roxy Theatres*, *supra*; 2 Glenn, *Mortgages*, Secs. 172.1 & 187), and if the loss is to fall upon him for whose benefit the receiver is appointed as suggested by those authorities, it should fall upon the mortgagee. (N. B. Mr. Jones' footnotes have been put in the body of the brief in parentheses.)

v. *Masserene*, 2 Ball. & B. 55,⁴ except that Mr. Maddock cites in addition the case of *Rigge v. Bowater*, 3 Brown Ch. 365. The American Treatises follow the English. High, Receivers, sec. 270; Beach on Receivers, sec. 303.) In a recent case in Arkansas, it was held that the mortgagee, at whose instance the receiver was appointed, could not be held liable in case such receiver embezzled or otherwise wasted the rents and profits. (*Robinson v. Arkansas Loan & Co.*, 74 Ark. 292, 85 S. W. 413.) But on the other hand, in a comparatively recent case in New Jersey, the vice chancellor held that in such case the mortgagee must bear any loss caused by the defalcation of the receiver so appointed, and the insufficiency of his sureties. (*Sorchan v. Mayo*, 40 N. J. Eq. 288, 23 Atl. 479.) *The vice chancellor reviews and comments upon the authorities, and concludes that they do not support the contention that the mortgagee is not responsible.*" (Emphasis supplied.)

An examination of the case of *Sorchan v. Mayo* will show that, as Mr. Jones remarks, he did examine and comment on the authorities and concluded that they did not support the contention that the mortgagee is not liable.

It is no small wonder that *Sorchan v. Mayo* has not been cited more often than it has, for since that decision, so far as counsel for petitioners have been able to discover, there have been only two reported cases dealing with the question,⁵ the Arkansas case and *Livingston v. Bauchens*, 254 App. Div. 692, 3 N. Y. S. 2d 776. Of these, the Arkansas case did not cite the New Jersey case, but the New York case followed it.

⁴ As pointed out by Vice Chancellor Pitney in *Sorchan v. Mayo*, the case of *Hutchinson v. Lord Masserene*, 2 Ball. & B. 55 does not support the contention of the text-writers.

⁵ The paucity of authority on this question is probably due to the fact that usually an adequate bond is given and the receiver insures.

The note on the instant case in 30 *Va. Law Rev.* 498, cited by respondents, loses much of its force when it is considered how many erroneous assumptions appear in it. 1. The note assumes that this action was instituted in the Federal District Court. Nothing in the opinion would suggest that it was not a case which had been removed, and the record shows that the complaint was prepared for the Superior Court of Richmond County, North Carolina (R. 1), and it affirmatively appears from the stipulation included in the typewritten manuscript record (p. 14), that this action was instituted in the Superior Court of Richmond County and was removed to the Federal District Court on motion of the Federal Reserve Bank of Richmond. 2. The note assumes that jurisdiction was obtained because of diversity of citizenship. Federal jurisdiction was, in fact, obtained because the Federal Reserve Bank of Richmond is a party (Manuscript record, p. 14). 48 Stat. 184, 12 U. S. C. A., Sec. 632; see *American Bank & Trust Co. et al. v. Federal Reserve Bank of Atlanta*, 256 U. S. 350, 356-7, 65 L. ed. 983, 989, 41 S. Ct. 499. 3. The note assumes that the mortgages on the property in question were separately owned, one by the Farmers Bank & Trust Co., and the other by the Federal Reserve Bank of Richmond. There is nothing in the opinion in the court below to support such a view, and the record only shows one mortgage. (R. 3.) It thus seems clear that this Law Review note is hardly to be given any weight as authority.

V

RESPONDENTS' CONTENTIONS ANALYZED

The contentions of respondents may be summarized thus:

"The receiver is an officer of the court; therefore, the mortgagees may not be held liable for his negligence and the insufficiency of his sureties." This premise is itself a conclusion resulting from two other premises: "1. An officer of

the court cannot be the agent of the mortgagees. 2. The mortgagees can be held liable for the negligence of the receiver only on the ground that the receiver is their agent." It is with these last two premises that we disagree, for we have never contended that a receiver is not an officer of the court. We will discuss them separately.

In the first place, in the collusion cases (*Re Penny*, 10 F. Supp. 638, and cases cited in annotations at 84 A. L. R. 1463 & 90 A. L. R. 406), it is said that "receivers will be *regarded* as agents of the parties rather than as officers of the court." 45 *Am. Jur.* 109, Receivers, Sec. 129. (Emphasis supplied.) The statement is not that they cease to be officers of the court but that they will be "regarded" as agents rather than as officers. It would seem that the language would indicate that they do not cease to be officers of the court but that for the purpose of liability are treated as agents. Whether receivers in cases of collusion *are treated* as agents, or *are* agents, it would seem that there would be no reason why the receiver, in a case such as this, should not be regarded as the agent of the mortgagees since he operated under their direction and control. So, also, a court of equity might very well look through the receivership entity, as it will through the corporate entity, though as a matter of strict law (such as respondents would have applied in this case), the agent of the corporation could not be the agent of the parent corporation, for, in law, they are separate entities.

The second premise is more involved. As we pointed out in our first brief (p. 17), where one person controls a third person, he is liable for his torts regardless of whether or not the master-servant or principal-agent relationship exists. Thus, in a number of cases, a person has been held liable for the torts of a third person even though the third person was not his servant. See, for example, *Dillon v. Winston-Salem*, *supra*. The mortgagee could likewise be held liable on the ground that the receiver is appointed for his benefit,

even though the receiver is not his agent. The benefit test is suggested by all the textwriters, according to Mr. Jones,⁶ though they seem to misapply it.

VI

THE QUESTION OF INSURANCE

We do not contend that the mortgagees had any duty to insure, but we do contend that they had no right to prevent the receiver from insuring. Their act in so doing amounted to an independent tort. See pp. 9-10 of our petition in this case. We did not rely on *Thompson v. Phenix Insurance Company*, 136 U. S. 287, 34 L. ed. 408, 10 S. Ct. 1019, as holding that "a receiver is always bound to effect insurance on property in his possession," as respondents state on page 19 of their brief. In footnote 1, page 9, of the petition, we said: "See *Thompson v. Phenix Insurance Company* . . .," intending to indicate a statement or dictum to that effect. See *A Uniform System of Citation* (Cambridge, Massachusetts, 1936, Harvard Law Review Association), p. 3.

It is well known that a receivership is a harsh remedy. *Martin v. Jonas*, 210 N. C. 665, 188 S. E. 81; *Neighbors v. Evans*, 210 N. C. 550, 554, 187 S. E. 796. One of the harsh things about it is that it takes a man's property out of his control so that it is beyond his power to protect it, and yet, at the same time, because his property has been taken away from him, he is deprived of the pecuniary ability to protect it with insurance.

All the matters of omission with which respondents charge Robert L. Steele, III, in their brief are at best matters of contributory negligence, which, under Rule 8(c) of the Rules of Civil Procedure, must be raised by answer.

⁶ 3 Jones, *Mortgages* (7th ed.), Sec. 1537a; 3 Jones, *Mortgages* (8th ed.), Sec. 1954.

VII

CONCLUSION

Since the appointment of a receiver is a harsh remedy (*Martin v. Jonas, supra; Neighbors v. Evans, supra*), for the benefit of the mortgagee (*Kane v. Roxy Theatres, supra; Sorchan v. Mayo, supra; 2 Glenn, Mortgages, Sec. 172.1; 2 Clark, Receivers, Sec. 963a*), it would seem only just and equitable that the mortgagee who has sought this harsh remedy for his benefit should "take the risk of the solvency of the receiver" ⁷ and the sufficiency of his bond.

This case presents an important question as to the application of the Rules of Civil Procedure which has not been decided by this Court and about which there is confusion in the lower federal courts. Furthermore, the Circuit Court of Appeals failed to follow the applicable North Carolina decisions holding that a person who controls another is liable for his torts and that North Carolina will follow the weight of authority; for the weight of authority as hereinabove shown, is to the effect that the mortgagee must suffer the loss occasioned by the negligence of the receiver. The Circuit Court of Appeals likewise failed to follow the decision of the Supreme Court of North Carolina in *Vanstory v. Thornton*, 112 N. C. 196, 17 S. E. 566, 34 Am. St. Rep. 483, which holds that a person at whose instance a receiver is appointed must suffer the loss occasioned by his malfeasance.

Respectfully submitted,

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⁷ *Sorchan v. Mayo, supra.*

